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THE MONETARY SYSTEM OF CHILE

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The period of paper money as legal tender through which the country is passing at present dates from 1898. (Law of July 31, 1898.) Metallic circulation was re-established in 1895 (Law of February 11, 1895), and lasted only until 1898. This law of 1895 established in Chile the monetary régime of gold, the dollar of 0.59/9103 grams (or 18d) being the monetary unit. With this law passed away the old bimetallism of colonial origin. The monetary system of to-day is thus nominally that of the gold standard established by the law of 1895, but superseded by paper money as legal tender. The monetary unit, therefore, is the paper money dollar, whose nominal value (at par) is eighteen pence, but whose real value in the markets of international exchange is very different. After these general explanations about the national monetary system, we may pass to a rapid survey of the more important economic characteristics of the legal tender in this last period—that is since 1898.

I. *The First Issue of Paper Money in 1898*

The régime of gold had been established in 1895 in the midst of a panic characterized by an increase of interest on money, the stagnation of business, failures and disastrous liquidations, the failure of many banking institutions, the decrease of the prices of town and suburban properties, of bonds and stocks, etc. The change of the monetary system also aggravated the crisis.¹ Strained conditions in our international relations, especially with the Argentine Republic, which caused great alarm, came coincidently with this critical situation of the economic state. The danger of war became more imminent each day, and tended to aggravate the economic situation, since the public was convinced that the declaration of war would also mean the declaration of a legal tender. The persistency

¹ "The Paper Money in Chile," by Dr. William Subercaseaux, Santiago, 1898. Similar account in "Le Marché Finance of 1898," by M. Raffalovich, Paris, 1899.

of the government in maintaining this reform withstood all outside pressure until June, 1898, at which time the danger of international conflict reached its culmination. The rumor began to spread in Santiago that the government was preparing to return to a legal tender basis, and, as a consequence, the bank depositors began to withdraw their deposits in order to save their gold. They did not try to exchange bank notes for gold, since there were no bank notes in circulation. Soon this movement spread and caused a run on the Santiago banks, which in less than two days placed these institutions of credit in a most precarious condition.

This panic was confined to the capital of the republic; in Valparaiso and in other cities the position of the banks was not affected. The banks of the capital finding themselves unable to pay their depositors, and the panic threatening to spread throughout the republic, the government authorized these banks to close their doors. Following this a general extension was ordered for thirty days, during which period Congress should determine measures to meet the situation. After a lively discussion Congress decided upon the issuance of \$50,000,000 of legal tender notes. Thus, through the cause of the fall of the metallic standard, its replacement by paper money was made necessary in order to save the banks from an accidental run. It was not possible to think of importing gold from abroad in order to weather the storm of the panic; for the nearest available hoard of gold was in Buenos Ayres, which, since the range of the mountains was closed, was fifteen days distant. If the legal tender had not been restored the metallic circulation would have continued, but the principal banking institutions of the country would have failed.

The state of distrust prevailing during this hazardous stage of the internal crisis and international dangers created, upon the appearance of the legal tender, high premiums on gold. Before the factors appeared which resulted in the panic, every premium paid in order to acquire metal of international exchange seemed justified. In that way the principal fluctuations of the previous period were produced, as can be seen in the appended tables. It was the moral effect of an unfavorable impression concerning the monetary future, either because of international dangers or because of the small amount of confidence with which the legal tender note issue was received, that caused the premiums on gold. The greatest

increase in the premium of gold was produced in January, 1899, in consequence of a bill introduced into the Senate for the purpose of increasing the legal tender issue, which failed to become a law because of the opposition of the government. These wide fluctuations, caused by the uncertainty and distrust of the times, show the instability in such periods of the value of paper money in relation to gold.

The international difficulties which had so greatly influenced this situation were definitely settled during the month of May, 1902. The return of confidence is clearly shown in international exchange,² for the gold premium steadily decreased from that time. The crisis existing at the beginning of the legal tender period in 1898 began to abate in a short time, and then slowly and gradually subsided. Beginning with 1902, the movement toward a re-establishment of credit indicates the beginning of the new period of prosperity. And here, apropos of the great fluctuation of exchange in the first part of this period of legal tender, we may call attention to the distinction already made, with great truth by some of the paper money theorists,³ to the effect that the value of paper money as an instrument of internal monetary circulation of a country must not be confused with the premium on gold, that is, with the standard of international exchange. It is true that between both phenomena there are important relations that I cannot mention here, but it is also true that there is a distinction. It may happen that a great depreciation of the paper relative to gold might come as a consequence of heavy demands for gold or bills of exchange, and yet the value of the paper as a national monetary unit for transaction of domestic business, not related to foreign trade, might not suffer an equal depreciation; in other words, the prices of the merchandise not imported and other domestic wealth might not increase. In that way during the first period extending from 1898 to 1902, the great increases in the premium on gold are not followed by proportionate increases, either of salaries, prices of town or suburban properties in the rentals of leases or of the prices of domestic products. As we shall see the depreciation of the dollar as reflected by a general increase of the prices resulted later.

² See table of premiums on gold.

³ Adolf Wagner, "Die russische Papierwahrung." C. Ferraris, "Moneta é curso forzoso." Milan, 1879. Lexis, Conrad's "Handwörterbuch."

We must observe, however, apropos of what has been said, that the influences which the premium on gold or standard of international exchange exercise in a country with paper money, depend to a large extent on the economic relations of this country with foreign countries. In Chile, as a consequence of the necessity of importing from foreign countries a large part of the products necessary for life—such as clothing and the different manufactures of silk, linens and wool—the depreciation of paper money relative to gold has a greater influence in the general monetary valuation than it would have in the case of products of prime necessity by itself. In the case of necessities of life, wide fluctuations of exchange are felt very directly amongst ourselves when they last for a fairly long period.

II. *The Period of Prosperity that Followed the Panic*

The economic crisis that made its painful ravages felt with such force from the years of 1894 until 1901 had been subsiding little by little, like the gradual healing of wounds. The premium on gold was disappearing rapidly⁴ as the probability of peace with the Argentine Republic approached nearer and nearer to certainty. In January, 1901, it had fallen to 2.6 per cent, but it again increased until in the first months of 1902, when the condition of our international relations again inspired distrust, it had passed thirty per cent. Beginning in May of that year, the dispute over the boundaries with a neighboring republic having been definitely settled, the premium on gold began to decrease once more.

When the legal tender currency was increased in 1898 the law directed that the customs duties on imports should continue to be paid in gold coin. The state changed the gold thus received for legal tender paper money, and in this manner a small quantity of gold which remained without monetary employment on account of the legal tender of the paper money was kept in circulation in the country. This was a measure which had no solid justification since the government did not need the gold collected in its custom house to make its payments abroad. Moreover, this measure, which took away from the paper money its financial support, tended all the more to depreciate it.

The greater part of the gold existing as circulating medium in

⁴ See appended table.

1898 was exported to foreign countries, contributing in this manner to create a balance of trade with foreign countries favorable to this country. The Argentine conflict once terminated, the financial situation which was produced was not considered dangerous; the premium on the gold—continually diminished toward the end of 1904.

At the same time that the financial position of the legal tender notes was being adjusted in such a satisfactory manner, the settlement of the crisis was turned day by day into a period of economic reaction. In place of the desperate depression of former years, signs of activity were now noticed and new fields of wealth and production opened to the country a larger route to progress. In the barren regions of the north important nitrate deposits were discovered, such as those of Antofagasta, Taltal and Aguas Blancas, which invited domestic and foreign capital and led to the formation of new companies for the exploitation of the nitrate beds. In the southern regions, and especially in the lands of Magallanes, the sheep-raising industry produced magnificent results, demonstrating the great value of fields almost wholly unused up to that time. This reaction continued until the end of the year of 1904, when a period of bourse speculation was introduced into the modest economic life of this country. Gold had a premium of less than seven per cent, and the financial condition being stringent, it being felt that the development of business would not adjust itself to the inelastic "\$50,000,000 legal tender plan," which constituted the only circulating medium since 1898, a movement for improving the situation was at once inaugurated, and Congress and the executive department decided to take up the matter. The banks complained of the decrease in their deposits, and it was noticed that the new impulse given to business required an increase of currency. How could this problem be solved? The creation of a convertible fund, a device tried with success in the Argentine Republic, was proposed by some; that is to say, a fund for the purpose of issuing notes in exchange for gold at par and of refunding gold in exchange for notes when the latter should be solicited. Others advocated an increase of legal tender notes. The latter idea triumphed and the government itself presented to Congress a project for their issuance, from which resulted the law of December 29, 1904, which author-

ized \$30,000,000 in fiscal notes, which in addition to those of the former issue made the total of circulating notes \$80,000,000.

This was without doubt an unfortunate solution of the agitation resulting from the financial stringency. Exchange was almost at par and the same financial limitation that was felt in the middle of that reaction, so favorable to economic life, would have brought as a consequence the easy operation of the convertible fund, and in this way the circulating medium would have received that elasticity which the legal tender lacks. Only in the presence of a certain necessity for circulation and with exchange at par, does a very favorable occasion present itself to sell paper at a par with gold. In 1904 the situation was such that without an increase in the issue, even if the convertible fund had not been created, gold would have been circulating at par with the notes, thus completing the circulating medium that was beginning to be too inelastic for the new situation.

The procedure of increasing the note issues on one side and, on the other, of depositing in the banks the sums issued, had the effect of lighting the fire of stock speculation. In contrast to the quiet and consistent course along which the settlement of the old crisis had been going up to the present time, the increase in the note issues and the fiscal deposits in the banks lent wings to the violent speculative movement which ushered in the new period of prosperity and progress. In "El Ferrocarril" of December 2, 1904, I wrote the following in regard to this question: "It cannot be denied that that was a very favorable occasion for the re-establishment of exchange at par without injuring debtors or creditors. But we must not deceive ourselves. This method that so clearly presented itself six months ago to-day meets new obstacles, which have since intervened,—and it is hard to admit it—in consequence of the project of Minister Sr. Ibanez.⁵ In truth this project was the starting of the real metamorphosis in the turn of business; it was the falling of a curtain separating two acts in the economic life of the country. Although the past crisis had disappeared, the raven and other birds of prey were still flying over their camp of spoliation, but a more promising outlook was now clearly perceived. The nitrate business promised a magnificent future and in Magallanes a new field of production had opened up.

⁵ Project of Issue.

"The reaction commenced gradually but on a quite solid basis. The appearance of the scheme of the government came to hurry the evolution and to convert it into an unbridled speculation. A few years ago, in 1894, the financial policy of the country went to the other extreme; in the midst of a very grave economic crisis and of international difficulties the monetary conversion was effected, producing a high valuation of coin and all the consequent effects of restriction. To-day, in 1904, in the midst of one of the most flourishing movements of prosperity that the country could have, the issue is increased, the government thus contributing in a most efficient way to separate us from the free circulation at par of outstanding notes." In the same article mentioned above, I said the following: "All this comes not from the fact that the paper is in itself a detestable instrument of circulation but from the detestable use that is made of the paper money."

With this policy of increasing the issue, one of the most favorable occasions that could present itself in order to regularize a circulation of our paper money at par was lost, and it contributed to favor the exchange of paper money for coin in its most dangerous form, upsetting the true movement of prosperity that was moving along on a most solid, though less violent basis. During the month of May, 1905, after the speculative fever had reached its height, following the most unheard-of development and abuse of credit, a sort of panic made itself felt, which resulted in the failure of many speculators. The banks restricted credit and speculation was thus paralyzed. It became impossible to form new companies, and many of those already formed commenced to fail. Exchange quotations fell sharply.

The reaction continued in this manner for a few months, but soon new symptoms of improvement were noticed. It is true that on the one hand the speculative fever and the abuse of credit were able to bring very grave consequences to the general condition of business, but it is also true that there was actual and effective wealth in many of the newly formed enterprises, and this wealth manifested itself sufficiently to prevent the appearance of a new crisis. The evidences of revival continued and new companies were created, whose securities underwent an increase in value similar to that of the older securities.

At the end of April, 1906, the banks again began to complain

of the lack of currency. A decrease in deposits was noticed which began to alarm some of our strongest banks. The rumor spread that the banks would even have to close their doors if the issue were not increased. The notes on deposit in all the banks as appears in a report of the Minister of Finance were:

January 31, 1906	\$34,335,219.06
February 28, 1906	25,735,428.01
May 31, 1906	22,228,408.22
In the month of April the decrease was much larger.	

Some again suggested at this time the establishment of convertible funds, with the power of issuing notes against gold, and the government respectfully presented the plan of a law; but as the gold was now at a greater premium, the normal operation of a scheme for supplying the market with the cash that it lacked was not so easily attainable.

Comparing the situation in 1906 with the one that existed in 1904, we find that in 1906 the speculative fever and the abuse of credit had not gone so far, so that it was much easier to adopt a monetary financial policy of resistance to the increase of the issues because no interests were bound to the depreciation.

This policy would have then, in 1904, tended to impede the development of speculation, which afterwards took a most violent character.

By 1906 circumstances tended unfavorably to the scheme of the convertible fund as a solution of the problem of financial stringency. Besides the depreciation of the notes, which hindered the normal operation of deposits—a new factor presented itself which required an increase in the issues—that created by the unheard-of development given to credit and speculation. To this new situation many interests were related.

Congress after a lively discussion in April, 1906, approved a law for the increase of \$40,000,000 of legal tender fiscal notes. This law, as the preceding ones, also provided for the accumulation of a convertible gold fund in European and American banks as a guarantee for the paper money. Together with the former issues the total quantity of notes had now reached the sum of \$120,000,000. Following are some quotations of the fluctuations of prices in the bourse of Santiago:

Name of Compan	Quotations in						
	Jan., 1901	Jan., 1902	Jan., 1903	Jan., 1904	Dec., 1904	Feb., 1905	Feb., 1906
Bank of Chile	112	113	135	156	172	182	202
Saltpetre of Antofagasta	106	190	197	225	334	445	6
Sugar refinery, Vina del Mar	113	135	131	127	202	257	6
Commercial exchange .....	...	...	...	3,500	3,500	10,000	20,000
Grazing and farming, Chile- Argentine .....	...	...	...	...	48	140	155

In these quotations we refer to a few stocks of very important enterprises. The stock quotations register in this period hundreds of security issues formed over night by speculation.

TABLE OF BANKING MOVEMENTS COMPILED FROM FIGURES FURNISHED BY THE
CENTRAL OFFICE OF STATISTICS.

Year ending Dec. 31.	Capital paid.	Fund in reserve.	Deposits.	Advances in money, values, etc.
1901 ⁷	42,120,007	4,428,563	94,567,415	106,700,359
1902	53,360,110	5,124,603	141,342,115	173,101,964
1903	54,739,690	5,368,264	136,285,501	162,860,516
1904	65,352,047 ⁸	8,619,629	171,085,232	201,691,651
1905 ⁹	76,047,683	11,134,450	294,107,369	296,964,488

It is well to observe that it is not the entire amount of these security issues showing the formation of new corporations which represents new capital, for often corporations were formed on the basis of existing enterprises that belonged to individual owners or companies, and the corporations which increased their capital are also included in these figures. Thus a mining company that was established in 1900 with \$1,500,000 capital, was bought up in 1905 by another corporation having \$6,000,000 capital, with only the expense of \$1,500,000 more capital. Other corporations only collected part of their capital, but appeared to be authorized to act on the basis of their total. At any rate the table is indicative of the speculative movement and the stock fever.

⁶ There was an alteration of their stock in these companies.

⁷ In this balance the foreign banks are not represented.

⁸ In these figures the funds of future dividends of stockholders are included.

⁹ The data for this year are taken from the chart of the Secretary of Treasury.

TABLE OF VARIOUS CORPORATIONS APPROVED BY THE GOVERNMENT.

Year.	Mines and Metallurgy.		Farming and Grazing.		Insurance Companies.		Transport Companies.		Various other Enterprises.		Total Capital.	
	£	\$	£	\$	£	\$	£	\$	£	\$	£	\$
1900. . .	205,000	1,810,000	.....	.....	.....	2,097,500	.....	1,262,900	.....	230,000	23,000,400	
1901. . .	400,000	3,453,250	.....	.....	.....	360,000	.....	1,781,000	.....	475,000	15,044,250	
1902. . .	40,000	3,677,500	.....	600,000	.....	.....	.....	6,508,000	.....	40,000	10,885,500	
1903. . .	.....	6,700,000	.....	6,083,000	.....	500,000	.....	3,136,000	.....	.....	.....
1904. . .	815,000	9,153,000	180,000	16,755,000	.....	520,000	.....	6,015,000	.....	995,000	58,598,000	
1905. . .	4,272,240	21,010,000	690,000	52,900,000	.....	1,020,000	125,000	23,370,000	654,000	5,741,240	113,309,000	

This table shows the foreign commerce.¹⁰

Year.	Imports.	Exports.
1901	\$139,300,766	\$171,844,976
1902	132,428,204	185,879,965
1903	142,470,509	194,279,672
1904	157,152,080	215,997,784
1905	188,596,418	265,209,192
1906	225,265,516	271,448,216

To resume, it may be said that never had Chile, in its different periods of economic prosperity, passed through one that could equal the period that included those years. By coincidence, many facts tending to maintain this movement were united; the good condition of the price of salt, the rise in the price of copper, of tin and also of wool; the splendid markets that the new salt and mining enterprises gave to agriculture and national industries, etc. The prosperous and flourishing condition of business in North America and Europe, which notably contributed to maintain and assist the enterprises that were formed with the easy access to credit and capital, and even to promote these enterprises abroad.

To all these facts was added the policy of increasing the note issues, and the deposit of fiscal funds in the banks, which tended to encourage speculation, responsible later for so many failures.

The increase in prosperity continued in this manner until August 16, 1906, when the earthquake of Valparaiso occurred, giving a terrible blow to the economic vitality of the country and causing enormous damage over a large territory.

The earthquake was the first event that came to interrupt the advance in prosperity, though it is true that neither its effects upon the exchange rate nor upon the quotations of securities upon the bourse were felt at once with any great intensity. The premium of gold, which was around twenty-eight per cent before the earthquake did not exceed thirty-two per cent until two months later.

III. *The Period of Prosperity Gives Way to One of Panic*

Symptoms of difficulties in economic conditions were felt as early as the end of 1906 in the principal centers of the great business activity of previous years. Valparaiso and Santiago were

¹⁰ The commerce of the province of Tcana and the territories of Magallanes are not included.

the markets where most of the big business enterprises centered and also where the grave consequences of the forthcoming economic difficulties were felt with the greatest violence.

People again began to talk about monetary stringency, business no longer found the former facilities, stock quotations on the bourse began to fall and the sales of stock and bonds met with greater and greater obstacles.

The development of the nitrate business was made very difficult through the steps taken by the government against the incorporation of most of the new enterprises, which served as the basis of the dealings in securities during the period of prosperity, and which were the principal nucleus of those nitrate works which belonged to citizens of the country. The nitrate industry of Chile, the exportation of which exceeds the amount of two hundred millions per year, is the basis of public and national wealth.

In 1907 the economic difficulties increased, always being localized, as heretofore, in the centers of Santiago and Valparaiso, where the difficulties were felt with the greatest intensity. In the remainder of the country the agricultural situation was prosperous and the condition of the nitrate industry was also satisfactory. Copper brought the enormous price of one hundred pounds sterling per ton. In a word the staples of production did not cause any anxiety. The difficulties had their beginning in the lack of capital to form and develop the unlimited number of enterprises which had been created in such a short space of time. It is doubtless true that the foundations of domestic capital were insufficient when compared with the size of the investments. The moment had arrived in which the great funds of capital, to which many had unconsciously contributed, had to be disbursed; the first dividends had been paid without difficulty, but now it was very hard to accumulate enough money for a like purpose. Many business enterprises without a solid foundation, some of those that started at the height of the investment fever, were already dead, and nobody thought of attempting to resuscitate them. They had, nevertheless, left behind the consequences resulting from the loss of great capital and large credits which had been granted them. It was understood that many of the vain hopes entertained about certain enterprises were doomed to destruction, but it was thought that the bases of those left were sufficiently strong to sustain economic prosperity.

In this year of 1907, while Minister of Finance, when the debate on the economic situation was opened in Congress, I said at the session of June 20: "We undertook to build up larger enterprises than domestic capital could support. But as this is not the moment to study what we have done in the past, we must consider only the method by which we may remedy the evil, because together with many enterprises which were formed without any basis whatsoever there are others which rest on a solid foundation, capable of contributing to our national prosperity."

I referred primarily to the nitrate industry in which many millions were invested and in which were felt difficulties due to lack of funds to finish and complete the new and valuable installations created.

There were at this time two dominant opinions among those interested in economic questions. A few considered that the government ought not to intervene in the matter, leaving everything to the initiative of the individuals, and this had been also the opinion of my predecessor in the ministry; the greater part, partisans of governmental intervention, again maintained that it was necessary to increase the note issue. I did not belong to either of these parties, but thought the government could lend its very valuable aid to the amelioration of the economic situation and ought to interest itself in so doing; I did not believe, however, that the government ought to have recourse to a new note issue. I indicated at the time the only remedy which would readjust business. Since the malady consisted in the lack of capital, it was necessary to provide it, and I proposed to bring back to the country the conversion funds which were being accumulated in European banks at three per cent interest, thinking it would be best to buy with them short term national bonds, including nitrate bonds, as is done with the "debentures" in London.

It was impossible to think of conversion, because the paper peso was greatly depreciated; on that account it was necessary to wait for a better opportunity to re-establish exchange at par. Nothing would be lost, therefore, if these funds were invested in bonds. In order not to withdraw these funds from the object for which they were intended, gold bonds would be created, that is to say, debts which the nitrate operators or the farmers would have to make payable in gold and the products of which in interest and

amortization would accumulate in gold, thus re-establishing the fund for the conversion.

The short term nitrate paper bond, say from eight to ten years, for example, lent itself very well to this operation, and as the product of these industries is for exportation it was convenient for those promoting such a business to make their debts payable in gold. To summarize, I thought that the only way to soften the effects of the crisis which presented itself in such alarming aspects was to secure capital for the development of the national enterprises which needed it. As the government had at the time a good sum of money inactive in foreign banks (more than 70,000,000 gold pesos worth 18d.) the intervention of the government could have resolved itself to the restoration of these funds to the country as long as the crisis lasted. If this were not done, the only alternative was that of a loan, but it was more economical to use the funds which were placed abroad at an interest of three per cent for this purpose leaving the question of a loan for the time in which the paper should be exchanged for gold money.

To this way of settling the affair, the opinions of many leading men were opposed. It was generally considered that it was better to increase the issue of paper money guaranteed with gold in Europe instead of touching this conversion fund, and, with this object in view, those that called themselves enemies of paper issues proposed to contract a loan abroad, to increase with it the conversion fund deposited in Europe, and to issue here in the country the corresponding paper notes.

Which was the way that would have carried us easier to the *desideratum* of arriving at a currency of paper money at par with gold, the increasing of a conversion fund, increasing at the same time issues of legal tender, or the avoiding of new issues by placing at a certain rate of interest in the country the funds set aside for the conversion? It is clear that the second way would more nearly avoid a still greater depreciation of the legal tender note, and this is the only way in which we could have carried the currency at par. Our notes were not then depreciated because our government had not funds enough to attend to their conversion. The government had sufficient means to establish either the exchange at any time, or a bank for conversion, like that of the Argentine Republic; but the low international exchange or the high premium of gold was

opposed to this. In other words, the currency at par of the legal bill could not be re-established, because it would have produced an economic panic by thus raising suddenly the monetary unit; but on no account was this due to a lack of funds. Each increase in the premium on gold was a new obstacle to a re-establishment of the normal currency of the legal tender note at par with gold and it was useless to have government funds ready for the conversion if further depreciation of these notes was inevitably coming to prevent such a conversion.

International exchange was already as low as twelve pence per peso, the value at par being eighteen pence, and it was seen that it would still decrease in value, and it can be seen that any new issue, even if guaranteed by gold deposits, made more and more unlikely the prospect of securing in the near future a currency with a rate of par between the peso note and the gold peso. But this was of small moment, as everybody was obstinately in favor of the guaranteed note; just as if the sole factor of the value of the note in relation to gold was the guaranty that it could be converted into specie, forgetting that the depreciation of the legal tender note meant as much as a declaration that although there was a possibility of redeeming it the government would never be able to fulfil this obligation.

One of the characteristics of the situation was the continuous fall of the rate of international exchange or the increase in the premium on gold, a situation which was derived from a constant demand for bills of exchange, which had been created by the new business enterprises, and in part by the earthquake. The nitrate works had to pay for machinery purchased abroad, and this was also true of the numerous new smelting works. Chileans had also bought up valuable foreign property, such as tin mines in Bolivia, and agricultural lands in the Argentine Republic and the necessity of paying for these acquisitions or of working them was naturally shown in constant demands for bills of exchange.

It can be seen consequently that the paper note was an instrument of currency which was insufficient to satisfy international obligations, and the solution suggested of increasing the paper issue could not satisfy the necessities arising from the lack of capital.

If it were thought to solve the problem of the lack of capital by means of a new issue, it is evident that the danger would be

created of increasing the premium on gold, which at the time was already sufficiently high.

I do not wish to give the impression that I believe that every increase of an issue of paper money is always accompanied by its depreciation in relation to gold, but, there are evidently indirect relations, dependent upon circumstances, which may cause a depreciation in relation to gold as a consequence of an increase of paper issues.

In the present instance, it is evident that if paper money were given to those who had to cancel obligations abroad, they would have to purchase bills of exchange, thus producing a fall in the rate of international exchange. On other occasions, as for example in 1898, the announcement of a new issue produced a fall in the rate of exchange through other reasons; the bad state of our foreign relations had filled people with distrust, further depreciation was feared, and naturally a great demand for bills of exchange was felt. These are examples which go to show how an increase of paper issues can, according to circumstances, have a direct effect upon international exchange.

"If we now set aside international exchange and simply look at what we might call the internal value of our monetary unit," I said, as Minister of Finance, to the Chamber of Deputies, "a value which is reflected in prices which have no relation to importation, as rent, salaries, prices of natural products, properties, etc., etc., we can establish, without recurring to voluminous statistics, the fact that there is a great decrease in the purchasing power of our money, in other words, the value of our money has decreased. It is true that in proportion to the increase of prices the prosperity of business has increased and has come to contribute to the demand of merchandise and to the increase of wages. Do not imagine therefore that I believe that the only cause for this phenomenon is the decrease in value of our legal bill."

"What would be the result of a new issue on the internal value of our peso? The old quantitative theory, according to which every increase of the amount of currency would have to be followed by a proportional decrease of its value, is, it is true, no longer held in modern economic science. It cannot be said, for example, as stated by Courcelle Seneuil, that if an issue is increased from 100 to 150 the value of the bill will decrease one-third; but it is

also true that the underlying principle of this theory still has to be taken into consideration, and it is the one which establishes that it is impossible constantly to increase the issues without decreasing the value of the bill or, in other words, that the increase of paper issues always carries with it a tendency to decrease the value of the money."

"It is necessary for us to remember in connection with the scarcity of currency which we note to-day, that as the value of our money decreases, even if we increase the paper issues, the feeling of stringency would continue to increase, because with the decrease of the money the necessities which we could before satisfy with 100 pesos would have to be satisfied with 120. This we have seen has happened during the last few months, for we must remember that a crisis and monetary stringency may be produced even under the régime of a paper currency, because if the increase of paper issues were always the remedy for such situations, this method would possess the valuable property of quenching all these irregularities of economic life. Let us remember, for example, that the Argentine Republic became involved in 1890 in a great economic crisis, although it was under the regimen of legal tender bills, and although the value of the bills was considerably decreased a great many cases of bankruptcy and business liquidation occurred, the prices of properties increased, interest on loans, etc., went up, and in a word, all the characteristics of a great panic were present."

Although I insisted that the ideas proposed by me should be followed, the resistance was so great, on the part of the executive against the bringing into the country of the funds deposited in Europe, and on the part of Congress against the same plan and in favor of the increase of the paper issue, that I convinced myself of the impossibility of putting through my plans. I attempted to retire from the cabinet, but the desire to serve my country with a program which I thought was convenient and sane, made me continue in the cabinet, on condition that a plan based on those same ideas be adopted, even if the funds deposited in Europe should be left untouched. The plan on which the government came to an agreement consisted in the following: In accordance with the dominant idea, it was declared that the government considered it expedient to intervene in the economic question, and that it would adopt all necessary measures to remedy the situation.

As the one remedy which is indispensable in such disorders of the economic organism is capital, money of international value, and not issues of paper money, it was decided to discontinue the remittance of the funds which were sent every month to Europe to be immobilized. The proceeds of these funds, which were not to be sent to Europe, and of a foreign loan, would be placed on the market together with some other gold certificates which were at the disposal of the government; and in order to adopt a just and appropriate method for handling these loans, there being no state bank and it being impossible to deposit more funds in the national banks, it was decided to buy bonds upon a territorial mortgage and nitrate bonds.

Though in former years of prosperity, and especially in 1904, as I have proved already, the economic evolution could have been brought about without the intervention of government capital, to-day things were changed. A new and terrible panic was menacing us and we could not abandon the prosperity offered by the nitrate enterprises and the new agricultural enterprises and others which possessed a real and positive basis of wealth. Then also through the initiative of the government a bank or rather a mortgage-loan institute, to facilitate the loans of the nitrate enterprises, was created, with bonds or debentures of short term. The mortgage-loan institute had been used for many years with great success as a governmental institution, and this new step was taken in favor of the national nitrate industry.

Once this plan had been agreed upon, the discussion of it began in Congress. The great majority in Congress were partisans of an increase of the paper issue, and it was soon seen that it was impossible to resist this majority without making the country endure the heavy consequences of a conflict between the executive and Congress. The legislative measures adopted after long discussions in parliament were the following:

1. The payment of importation duties in gold was suppressed. This measure stopped anomalous circulation of specie within the circulation of depreciated paper money.
2. It was arranged that notes be issued in exchange for gold, that is to say, that a note be given in exchange for each gold peso of eighteen pence deposited.

This measure had no importance at this time, because of the depreciation of the paper peso in relation to gold, but it was adopted

as an inoffensive measure to be applied when exchange should improve.¹¹

3. The nitrate mortgage-loan institute was created for the issue of special bonds or debentures for this industry.

4. The accumulation of funds for the conversion of legal tender notes in Europe was suspended; the government was authorized to complete this fund by means of a loan when the conversion of the notes should be made.

5. An increase of the legal tender notes was made to the amount of \$30,000,000, even against the opposition of the executive. This sum was created for the purchase of mortgage bonds.

6. The executive was authorized to contract a loan of three million pounds sterling to be devoted later to the construction of public works, to be invested meanwhile in bonds.

The purpose of this loan was to avoid a still greater depreciation of the paper money, by placing in the country a great amount of bills of exchange and placing these funds for some time in the country through the purchase of bonds. It was understood by many that with the issuance of only paper money, international exchange would continue to fall, because great sums of money had constantly to be sent abroad. As it can be seen, the legislative measures adopted by Congress did not correspond to the plan or project approved by the government. Nevertheless we did all we could to obtain the object which we had in view as a remedy for the panic, even without going beyond the legislative measures adopted, there being in the law sufficient material from which a solution of the situation could be worked out.

In this I met with serious opposition in the government and after my resignation from the ministry, the program proposed by me was completely abandoned. The foreign loan was not contracted for the whole amount, and it may be said that the issue of \$30,000,000 was the only means adopted for the creation of money-capital.

At the end of 1907 it was seen that the general economic situation was getting worse and worse, and the panic was approaching with disastrous outward manifestations. The panic in the United

¹¹ The reason for choosing this occasion, which was so inopportune, to provide for the issuance of notes against gold was that a group in Congress tried to create a Bank of Issue against mortgage bonds, so that everybody who deposited bonds could obtain bills. The government then declared that it would permit issue only against gold and not against bonds.

States and its echo in Europe helped to complicate the situation in Chile. Strong foreign houses and banks, which had capital in the country, began to demand the payment of their credits. This and the numerous debts contracted here in previous years, as a result of the many new enterprises which had recently been undertaken, made the question a very serious one.

Following the panic in the United States and Europe the situation in Chile became alarming. International exchange fell rapidly, and numerous business houses went into bankruptcy and insolvency, and these produced the consequent business panic. The effects of the panic were felt principally in Valparaiso and Santiago, which have been the great business centers of late years. Few of the numerous securities quoted on the bourse in previous years now found buyers. The risky enterprises which had been formed for the sole purpose of speculation had disappeared some time before, and the shares of the stable enterprises began to suffer heavy losses in their prices. Happily the panic did not yet extend to agriculture, but agriculture was not sufficient to heal the gaping wounds left by the new situation.

The force of circumstances had compelled the government to recognize, although somewhat too late, the gravity of the situation, of the nitrate enterprises, and especially of recently discovered nitrate in Atacama. With the funds at its disposal and through our principal bank it had tried to make loans to these enterprises, and keep them from stopping their works. But this method, had not only come too late, but had also had all the disadvantages of a measure which was poorly studied and applied, and which had not been carried out with a general spirit of justice and equity. To-day it is being recognized that the policy of placing national funds in nitrate bonds would not only have been efficacious, but would have been more just as a protection to this important branch of the national industries, which from a financial point of view produces more than fifty per cent of the public income of the nation, while of the total amount of our exportation it produces eighty per cent. As far as the nationalization of this industry is concerned our policy could not have been worse.

What, it may now be asked, ought to be our financial policy in the future? In the year 1910,¹² the term fixed for the redemption of

¹² This paper was written at the close of 1909.

the legal tender bills by gold pesos of eighteen pence will cease. Since the legal tender note is now considerably depreciated in relation to the gold peso, and considering the long time in which the contracts have been adapting themselves to this situation, it is easy to understand that it would not be possible to redeem the currency in 1910 without greatly endangering the development of business. If, as far as the means at the disposal of the government are concerned, the operation were possible, considering the effects it would have on the development of business, on credit, on the fulfilment of contracts and on the stability of banks, it can be said with certainty that grave dangers would arise which ought to be avoided. For the re-establishment of the metallic currency an occasion must be selected which ought to correspond to a period of actual economic prosperity, as was for example that of 1904. It is known with what distrust the public would, after a complete failure in the year 1898, receive the conversion of the legal tender notes. It is therefore necessary to carry out such an operation in times of prosperity, when the wounds of the present crisis are healed, and when new vigor and life animates the financial situation of the country.

It can be seen therefore that a conversion at par or at eighteen pence is not likely to be carried out, and therefore the authorities ought to begin to think of setting a lower rate of exchange for the gold which would replace the notes; this rate could be fixed for example at twelve pence. But this operation would have the disadvantage of reducing still more the value of our peso, and for this public opinion with us does not as yet seem to be prepared. If the depreciation lasts for some years longer a unanimous opinion on this point could perhaps be secured. It might be urged in favor of this measure that it would be better to have a fixed value for the peso at twelve pence instead of a nominal value of eighteen pence, which in reality changes continually in its relation to gold and costs to-day only nine pence. It was in this manner that the Argentine Republic settled its financial difficulties through the bank of conversion. But even in this case better times would have to be selected for the operation, as was done in the Argentine Republic. The exchange of the day of the conversion was selected for the permanent one and consequently no harm was done to debtors, the operation being received without distrust, as would happen if the exchange selected were higher than the actual international exchange. Our exchange to-day being as low as nine pence, it would cause

panic and unnecessary trouble to raise it to twelve pence. Our financial policy then must confine itself now to leaving things as they are. Let us wait for better times without increasing the paper issues, and I do not doubt that a day will come in which it will be sufficient for the government to establish the exchange of the gold and legal tender note at par. The circulation of the note and gold at par can be arrived at by establishing the exchange at sight and to the bearer; and here where the people are accustomed to the notes it would be sufficient to leave to the government the power of making issues. In this case we would have gold money, supplemented by paper bills which would circulate at par with the gold.

The solution of the financial difficulties in the Argentine Republic with the bank of conversion depends upon a mixed circulation of gold and paper, the latter being exchangeable at sight and to the bearer. The gold does not circulate as it does in Europe or the United States, that is to say as in those countries which have a gold unit, but it circulates in the form of paper, the gold being left on deposit in the bank of conversion and its coinage being thus avoided. Both solutions are similar, but both must be established in prosperous times and when the wounds of the present situation are healed—that is to say, when they would not produce fluctuations dangerous to business.

Let us devote ourselves at present to effacing the difficulties of the present situation, and let us work for the development of those enterprises which constitute the basis of our national wealth. Let us take those measures which are necessary to bring about this evolution, and when the wounds are healed, the solution of the financial crisis will come about without friction.

AMOUNT OF PAPER MONEY IN CIRCULATION.

Year.	Issue.	Total in circulation.
1898	\$50,000,000	\$50,000,000
1899	50,000,000	50,000,000
1900	50,000,000	50,000,000
1901	50,000,000	50,000,000
1902	50,000,000	50,000,000
1903	50,000,000	50,000,000
1904	30,000,000	80,000,000 (Law of Dec. 29)
1905	30,000,000	80,000,000
1906	40,000,000	120,000,000
1907	30,000,000	150,000,000

PREMIUM ON GOLD.

(Table taken from the quotations of the bourse as published in *El Mercurio* and *El Ferrocarril*.)

Year.	Month.	Premium on gold in %.	Year.	Month.	Premium on gold in %.
1898	August 14	.....30	1900	Jan. 30	.....11
1898	August 15	.....46	1900	Feb. 14	.....10¼
1898	August 17	.....37	1900	Feb. 28	.....11.20
1898	Sept. 10	.....25	1900	Mar. 14	.....9½
1898	Sept. 14	.....40	1900	Mar. 31	.....9½
1898	Oct. 10	.....26½	1900	Apr. 15	.....9¾
1898	Oct. 14	.....32½	1900	Apr. 30	.....8½
1898	Oct. 31	.....34	1900	May 14	.....8
1898	Nov. 14	.....35½	1900	May 31	.....5½
1898	Nov. 30	.....38	1900	June 15	.....3¾
1898	Dec. 14	.....39	1900	June 30	.....3
1898	Dec. 31 ¹³	.....44	1900	July 14	.....3¾
1899	Jan. 14	.....49	1900	July 31	.....3½
1899	Jan. 30	.....39½	1900	August 14	.....3¾
1899	Feb. 14	.....38.80	1900	August 31	.....3¾
1899	Feb. 28	.....35	1900	Sept. 14	.....3¾
1899	March 14	.....32	1900	Sept. 29	.....2½
1899	March 31	.....29½	1900	Oct. 15	.....5
1899	April 10	.....32	1900	Oct. 31	.....5½
1899	April 14	.....24¼	1900	Nov. 15	.....5¼
1899	May 14	.....22¼	1900	Nov. 30	.....5¾
1899	May 31	.....24	1900	Dec. 15	.....5¼
1899	June 14	.....18	1900	Dec. 30	.....2½
1899	June 30	.....19	1901	Jan. 14	.....2
1899	July 14	.....18	1901	Jan. 31	.....4
1899	July 31	.....15½	1901	Feb. 15	.....8
1899	August 14	.....15½	1901	Feb. 28	.....5½
1899	August 30	.....16½	1901	Mar. 15	.....4½
1899	Sept. 14	.....16½	1901	Mar. 30	.....5
1899	Sept. 30	.....17½	1901	Apr. 15	.....5½
1899	Oct. 14	.....19	1901	Apr. 30 ¹⁴	.....9
1899	Oct. 31	.....23¼	1901	May 17	.....9¾
1899	Nov. 14	.....20¼	1901	May 31	.....14
1899	Nov. 30	.....16	1901	June 15	.....12¾
1899	Dec. 14	.....14	1901	June 30	.....13
1900	Jan. 2	.....9	1901	July 15	.....13¾
1900	Jan. 15	.....10½	1901	July 31	.....14½

¹³ A project presented for the increase of the legal tender notes was presented by 15 Senators, but was not approved.

¹⁴ The President of the Republic turned over the public affairs to the Minister of the Interior on account of severe illness.

Year.	Month.	Premium on. gold in %	Year.	Month.	Premium on gold in %.
1901	August 14	10¾	1903	Feb. 2	9¼
1901	August 30	8½	1903	Feb. 16	8.90
1901	Sept. 13	10	1903	Mar. 2	7¼
1901	Sept. 30	13	1903	Mar. 14	8¾
1901	Oct. 15	12¾	1903	Apr. 10	7
1901	Oct. 31	15½	1903	Apr. 15	8.20
1901	Nov. 14	15	1903	May 1	7.80
1901	Dec. 22	17½	1903	May 16	8
1901	Dec. 14	23	1903	June 1	10
1901	Dec. 30 ¹⁵	26	1903	June 15	7.80
1902	Jan. 15	24	1903	July 2	7½
1902	Jan. 30	26½	1903	July 16	7¼
1902	Feb. 14	27.80	1903	August 1	8
1902	Feb. 28	27¼	1903	August 16	9½
1902	Mar. 15	31¾	1903	Sept. 2	9.20
1902	Mar. 31	29	1903	Sept. 16	8.80
1902	Apr. 15	29½	1903	Oct. 1	8
1902	Apr. 30	25	1903	Oct. 15	9¼
1902	May 15	23	1903	Nov. 2	8.40
1902	May 30 ¹⁶	13.40	1903	Nov. 16	8
1902	June 14	14	1903	Dec. 1	6½
1902	June 30	14¼	1903	Dec. 26	6½
1902	July 15	11½	1904	Jan. 15	7.30
1902	July 31	14	1904	Jan. 30	8
1902	August 14	12	1904	Feb. 18	8.20
1902	August 29	11	1904	Feb. 28	7½
1902	Sept. 14	11½	1904	Mar. 14	7¼
1902	Sept. 30	11.30	1904	Mar. 30	7¾
1902	Oct. 15	11.60	1904	Apr. 16	7½
1902	Oct. 30	11½	1904	Apr. 30	7¼
1902	Nov. 14	11¼	1904	May 14	6½
1902	Nov. 29	10	1904	May 30	6
1902	Dec. 15	7	1904	June 16	6
1903	Jan. 10	7½	1904	June 27	5.70
1903	Jan. 15	8	1904	July 14	6.80

¹⁵ The state of international relations with the Argentine Republic inspired new distrust.

¹⁶ The Argentine conflict was arranged finally.